Jay Bennett
Director
Federal Regulatory Relations

1275 Pennsylvania Avenue, N.W., Suite 400
Washington, D.C. 20004
(202) 383-6429
Fax: (202) 347-0320

PACIFIC TELESIS
Group-Washington

RECEIVED
MAR - 4 1996
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

March 4, 1996

RECEIVED
MAR - 4 1996
FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, NW, Room 222
Washington, DC 20554

DOCKET FILE COPY ORIGINAL

Dear Mr. Caton:

Re: *CC Docket No. 95-185, Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers*

On behalf of Pacific Bell, Pacific Bell Mobile Services, and Nevada Bell, please find enclosed an original and six copies of their *"Comments"* in the above proceeding.

Please stamp and return the provided copy to confirm your receipt. Please contact me should you have any questions or require additional information concerning this matter.

Sincerely,

Jay Bennett

Enclosure

No. of Copies rec'd 0+5
List ABCDE

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

RECEIVED

MAR - 4 1996

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

RECEIVED

MAR - 4 1996

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

In the Matter of	)	
	)	
Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers	)	CC Docket No. 95-185
	)	
	)	

COMMENTS BY PACIFIC BELL, PACIFIC BELL MOBILE SERVICES, AND NEVADA BELL

LUCILLE M. MATES
JEFFREY B. THOMAS
SARAH RUBENSTEIN

140 New Montgomery Street, Rm. 1529
San Francisco, California 94105
(415) 542-7661

MARGARET E. GARBER

1275 Pennsylvania Avenue, N.W.
Washington, D.C. 20004
(202) 383-6472

Attorneys for Pacific Bell, Pacific Bell Mobile Services, and Nevada Bell

Date: March 4, 1996

TABLE OF CONTENTS

Page

SUMMARY

The Telecommunications Act of 1996 (the "new Act") has removed the legal basis of this proceeding by delegating to the states all authority related to the LECs' negotiation of contracts concerning interconnection rates. The new Act expressly strips the Commission of the authority to mandate the terms and conditions of interconnection agreements. While the Commission is charged with establishing general rules governing interconnection, the specific terms and conditions of interconnection agreements are fashioned through negotiations by the parties, subject to arbitration and approval by State Commissions. 47 U.S.C. Section 252. The FCC is not permitted by the Act to interfere in this process. Moreover, as the Act makes clear, no regulator can mandate Bill and Keep arrangements. Such arrangements can arise only by agreement of the parties to "waive" their right to mutual recovery. Section 252(d)(2)(B)(i).

We agree with the Commission's general belief that change is needed in the framework for interconnection between LECs and commercial mobile radio service ("CMRS") providers. We support Mutual Compensation for this interconnection, under which each carrier recovers its costs of terminating traffic on its network for the other carrier, as is required by the Telecommunications Act of 1996. The Mutual Compensation that we support goes beyond the Commission's current requirements for LEC-to-CMRS interstate traffic. As we have pointed out before, the Commission's current access charge rules make its interstate Mutual Compensation requirement meaningless.

For traffic that does not involve an interexchange carrier, Pacific Bell intends to begin negotiating with CMRS providers in April of this year for Mutual Compensation agreements that will replace our current access charge-based agreements when they expire in April of 1997. It will take time to implement the change from our existing arrangements to Mutual Compensation because we anticipate that our end users also will face rate revisions as a result of the change. There is no urgency that warrants an immediate "interim" solution. We will, of course, make revisions consistent with the requirements of the new Act. In the mean time, our current contractual agreements with cellular providers are reasonable, and cellular providers in California have been flourishing while operating under them. The emergence of PCS does not create any urgent need for change. We offer PCS providers the same arrangements that have been negotiated with cellular providers, and PCS providers have been negotiating interconnection contracts with us.

By pricing termination at zero, Bill and Keep would create numerous economic distortions that would harm consumers and the industry. Bill and Keep would encourage arbitrage by subsidizing one technology, at the expense of others. Bill and Keep would leave CMRS providers with no economic incentive to expand parts of their networks where they can instead get a "free ride" on LEC investment. In addition, Bill and Keep would discourage Competitive Local Carriers and other competitors from building facilities for termination of CMRS traffic, since they could not compete with a LEC price of zero.

In California, approximately 83% of CMRS traffic originates on the wireless networks and terminates on the wireline networks, while only approximately 17% of the traffic flows the other way. Because of this traffic flow imbalance of over four to one, giving away terminating interconnection would create uncovered costs for LECs that are over four times greater than the uncovered costs for CMRS providers. Because of the traffic imbalance and its resulting cost imbalance, Bill and Keep would subsidize CMRS providers without any public interest rationale. Once established on an interim basis, it may be very difficult to remove because it will give the recipients of the subsidy reason to fight against its removal. Bill and Keep may become like the "temporary" ESP exemption from access charges that the Commission created to avoid "rate shock" in 1983, and which continues today in spite of the Commission's subsequent reviews of the exemption and proposal to remove it.

Requiring Bill and Keep with an interconnection rate of zero and without establishing a cost-recovery mechanism would be inconsistent "with meeting 'the minimal requirements for protection of investors' against confiscation that inhere in the statutory standard of just and reasonable rates." No matter how the Commission might structure an interim approach, that approach would interrupt our existing arrangements which are based on access charge principles. In these arrangements, we depend on compensation for originating and terminating access in order to have an opportunity to recover our costs. The charges have been negotiated as integrated packages, and we expect that revisions in the charges between the carriers will necessitate revisions in charges to end users. For instance, when we negotiated our Type 2A access-tandem interconnection, in order for the CMRS providers to increase traffic terminating to their networks, they requested pricing that allows landline end users to call CMRS end users from anywhere in a LATA without paying toll rates. For example, if a Pacific Bell residential flat-rate subscriber in San Francisco calls a CMRS customer in Eureka (300 miles away), today the Pacific Bell subscriber pays no charges in addition to those for basic flat-rate local service, which Pacific Bell prices at $11.25 per month.

We cannot quickly revise how we charge end users for specific calls. Thus Bill and Keep, Mutual Compensation, or other arrangements cannot be implemented quickly on an interim basis. Revisions in end user charges require us to take the following steps: 1) negotiate new arrangements with CMRS providers; 2) gain California PUC approval of the arrangements and any changes in end user charges; 3) obtain and install software translations in our switches; 4) unbundle charges for parts of our network in cases where CMRS providers currently have chosen to purchase services on a bundled basis; 5) provide notice to end users; and 6) modify our billing system to handle price changes.

The emergence of local exchange competition makes this a particularly inappropriate time for the Commission to rush into the adoption of an uneconomic approach for interconnection. If we and other LECs were to treat CMRS providers unfairly, we would be providing numerous local competitors all the more incentive to provide alternative interconnection arrangements. Instead, we are striving to meet the needs of CMRS providers so that they will build long-term business relationships with us.

Based on Dr. Gerald Brock's analysis, the proponents of Bill and Keep allege that the average long run incremental cost ("LRIC") of local termination on LEC networks is approximately 0.2 cents per minute. Brock's analysis is wrong; his estimates of LRIC are too low, and he ignores other relevant costs. Bill and Keep would prevent LECs not only from recovering LRIC but also shared and common costs.

With the explosion of competition in local exchange markets, regulators must allow economically rational pricing. LRIC, the added cost of producing an increment of service output, is universally recognized as the economically relevant cost for use in pricing, especially for setting price floors. Because of the LECs' economies of scope and scale and relatively high shared and common costs, pricing all LEC services at LRIC would not permit them to recover their total costs and would put them out of business.

In order to describe these pricing principles and their impact, we have attached as exhibits to our Comments two papers by expert economists: 1) Statement of Professor Jerry A. Hausman, MacDonald Professor of Economics at MIT (Exhibit B hereto); and 2) "Incremental Cost Principles For Local And Wireless Network Interconnection," by Timothy J. Tardiff, National Economic Research Associates, Inc., and Richard D. Emmerson, INDETEC Corporation (Exhibit D hereto). Professor Hausman also explains the economic distortions that would be caused by a Bill and Keep policy and how they would severely harm the industry and the public.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

RECEIVED

MAR - 4 1996

In the Matter of

Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers

CC Docket No. 95-185

COMMENTS BY PACIFIC BELL, PACIFIC BELL MOBILE SERVICES, AND NEVADA BELL

I. GENERAL COMMENTS

A. THE TELECOMMUNICATIONS ACT OF 1996 HAS MOOTED THIS PROCEEDING

The recent enactment of the Telecommunications Act of 1996 (the "new Act") has removed the legal basis of this proceeding by delegating to the states all authority related to the LECs' negotiation of contracts concerning interconnection rates. The states have the authority to make "determinations...of the just and reasonable rates for the interconnection of facilities and equipment."[1] When arbitrating contract disputes,

---

[1] Section 252(d)(1); see also Section 251(c)(2). The Sections that we refer to in these Comments are the Sections added to the Communications Act of 1934 and Title 47 U.S.C. by the Telecommunications Act of 1996, not the Sections of the new Act itself.

the states have the authority to "establish any rates for interconnection services...."[2] The states also have the authority to approve interconnection contracts adopted by negotiation or arbitration.[3] The Commission may intervene only when the state fails to act,[4] and there is no reason to believe that states will fail to act. Certainly, California and Nevada will continue to be actively involved with interconnection rates between LECs and providers of Commercial Mobile Radio Service ("CMRS").[5]

Even prior to passage of the new Act, contrary to the Commission's tentative conclusion,[6] it had no authority to preempt the states' regulation of the intrastate rates for LEC interconnection with CMRS providers. Section 152(b) of the Communications Act of 1934 reserves intrastate authority to the states. So long as the state regulation does not prevent entry and interconnection by CMRS providers, Section 332(c)(3), which was added by the 1993 Budget Act,[7] does not give the Commission authority over interconnection rates. In Louisiana PSC v. FCC, the Supreme Court upheld the states' authority where state regulation does not negate the Commission's ability to regulate interstate service in furtherance of its legitimate federal interests, including where interstate and intrastate service are severable.[8] In its NPRM, the Commission

---

[2] Section 252(c)(2).

[3] Section 252(e).

[4] Section 252(e)(5).

[5] See, e.g.. Investigation on the Commission's own motion into the regulation of cellular radiotelephone utilities, CPUC, I. 88-11-040, Decision 90-06-025, June 6, 1990.

[6] Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers, CC Docket No. 95-185, Notice of Proposed Rulemaking ("NPRM"), para. 111 (1996).

[7] Section 253(e).

[8] Louisiana Public Service Commission v. FCC, 476 U.S. 355, 375 n. 4 (1986) ("Louisiana PSC").

does not set forth any facts showing that the states' regulation of intrastate rates for LEC-to-CMRS provider interconnection negates the FCC's legitimate regulation in any way. Moreover, the locations of the origination and termination of calls involved in this interconnection are technically capable of being known by either the CMRS provider or the LEC, and thus regulation of the calls is severable between jurisdictions. The Commission could require declared PIUs where warranted. Or, in order to make reasonable, jurisdictional allocations easier to implement, it could adopt a surrogate, as it has in the past (e.g., the Entry-Exit-Surrogate[9]). A surrogate could measure a call from the first point of switching in the public switched telephone network ("PSTN").

Most important, the new Act makes it clear that the states' regulation of interconnection rates does not negate any federal interest, since the legislation itself establishes the exclusive state role over terms and conditions of interconnection.[10] Where the states carry out this regulation, the new Act not only prohibits preemption but removes the FCC's authority to establish rates. Accordingly, the Commission should either close this proceeding or keep it open solely for the purpose of helping the

---

[9] Determination of Interstate and Intrastate Usage of Feature Group A and Feature Group B Access Service, CC Docket No. 85-124, Memorandum Opinion and Order, released December 5, 1989 (the "Entry/Exit Surrogate or EES Order"). Under the EES method of jurisdictional determination, calls that enter an IXC network in the same state as that in which the called station is located are deemed to be intrastate, and calls that terminate in a different state than their IXC point of entry are considered interstate. Id. at n. 5. The Commission adopted this surrogate for FGA and FGB services, "that generally do not provide ANI capability," which is needed for the LECs to identify and measure jurisdictional usage.

[10] The Commission has the responsibility to establish regulations for interconnection agreements. The states must use those regulations in arbitrating negotiations, but the parties to the negotiations and the states are responsible for the terms and conditions, including rates, of the agreements. See Part II - B below.

Commission work cooperatively with the states and other parties to determine an improved framework for interconnection.

This cooperation would be consistent with the Commission's stated goals. In its NPRM, the Commission stated, "In determining what the Commission's role should be with respect to implementation of LEC-CMRS interconnection policies, we again emphasize our recognition of the states' legitimate interest in interconnection issues and our intention to work in coordination with state regulators in this regard."[11] Any attempt to preempt the states concerning this vital aspect of local interconnection would be incompatible with this desired federal and state coordination.

If we assumed, solely for the sake of argument, that the Commission could both regulate and preempt state ratemaking for LEC-to-CMRS interconnection, the Commission should still refrain from doing so, in order to avoid the creation of inefficient networks and uneven competition. It is undisputed that purely wireline switched service is severable between intrastate and interstate jurisdictions, and both Louisiana PSC and the new Act make it clear that the states cannot be preempted from ratemaking for wireline-to-wireline interconnection (e.g., LEC to Competitive Local Carrier, or "CLC," interconnection). If the Commission were to regulate and preempt solely LEC-to-CMRS ratemaking, the stage would be set for arbitrage, inefficiency, and unfair competition. For instance, the Commission might ill-advisedly order Bill and Keep for LEC-to-CMRS interconnection, but a state might order or allow Mutual Compensation for LEC-to-CLC interconnection. In that event, CMRS local providers would be advantaged over

[11] NPRM, para. 114.

wireline local providers. Also, there would be a strong incentive for arbitrage by wireline carriers to terminate their traffic for free via LEC-to-CMRS interconnection.

Since it is clear that the Commission cannot regulate and preempt the interconnection rates for all competitors in the local market, the Commission should avoid trying to regulate and preempt interconnection of one type of competitor. Allowing the states to regulate all the competitors in the local market equally will be consistent with Congress' intent in the new Act that regulation replicate competition and maximize benefits for consumers and society.

B. WE AGREE THAT CHANGE IS NEEDED IN LEC-TO-CMRS INTERCONNECTION, AND WE SUPPORT MUTUAL COMPENSATION, BUT THERE IS NO PUBLIC INTEREST NEED FOR AN "INTERIM" CHANGE

We agree with the Commission's general belief that change is needed in the framework for LEC-to-CMRS interconnection. We support Mutual Compensation for this interconnection, as is now required by the Telecommunications Act of 1996. The Commission describes Mutual Compensation, which is known also as reciprocal compensation, as follows: "This principle requires LECs to compensate CMRS providers for the reasonable costs incurred by such providers in terminating traffic that originates on LEC facilities. Similarly, CMRS providers are required to provide such compensation to LECs in connection with wireless-originated traffic terminating on LEC facilities."[12]

---

[12] Id. at para. 21. A change to Mutual Compensation, by itself, would not affect how CMRS providers charge their end users (i.e., "called party pays").

The Mutual Compensation that we support goes beyond the Commission's current requirements. The Commission currently requires Mutual Compensation for LEC-to-CMRS interstate traffic. As we have pointed out before, however, the Commission's current access charge rules make its Mutual Compensation requirement meaningless. All the traffic we carry that originates or terminates as wireless and is identified as interstate in nature is traffic for which we are providing access service to an IXC.[13] On that traffic, we are compensated solely by the IXC for providing the local transport portion of switched access. We neither seek payment from nor provide payment to CMRS providers that help originate or terminate this traffic, because they are providing portions of switched access for the IXCs, not for us.[14] Moreover, we do not receive compensation from the end-user for these calls.

For traffic that does not involve an IXC,[15] Pacific Bell intends to begin negotiating with CMRS providers in April of this year for Mutual Compensation agreements that will replace our current access charge-based agreements when they expire.[16] Currently, we have 24 contracts in place with cellular providers and one with an ESMR. These contracts expire in April of 1997, and we intend to have new contracts negotiated on the basis of Mutual Compensation at that time. On March 1, 1996, Pacific Bell sent a letter

---

[13] Approximately 16.5% (9.2% interstate plus 7.3% intrastate interLATA) of our traffic in California and Nevada that originates or terminates as wireless involves an IXC.

[14] For instance, on tandem routed calls, the CMRS providers perform local switching and carrier common line functions. In an end office arrangement, we perform local switching functions and charge the IXC for them. In either case, we receive no compensation from either the CMRS provider or the calling party.

[15] Approximately 83.5% of our wireless traffic does not involve an IXC.

[16] Nevada Bell has tariffs for wireless interconnection.

to all cellular and ESMR carriers in our territory informing them that we are preparing to begin a new interconnection agreement. We explained that we continue to be committed to an April 1996 start of a new round of negotiations that we expect will result in Mutual Compensation agreements. Our letter is attached as Exhibit A.

It will take time to implement the change from our existing arrangements to Mutual Compensation because we anticipate that our end users also will face rate revisions as a result of the change. There is no urgency that warrants an immediate "interim" solution. We must, of course, make revisions under the requirements of the new Act. As noted, we will retain our current access charge-based contractual agreements with cellular providers until they expire in April of 1997. The Commission should not disrupt or abrogate our contracts. They are reasonable, and cellular providers in California have been flourishing while operating under them. As Professor Hausman points out, "Cellular is the success story of telecommunication in the 1990's...."[17]

The emergence of PCS does not create any urgent need for change. We offer PCS providers the same arrangements that have been negotiated with cellular providers, and PCS providers have been negotiating interconnection contracts with us. Most are for one year terms only and will expire at the same time that we expect to be replacing our existing cellular contracts with contracts negotiated on the basis of Mutual Compensation. In any event, once we have made the needed changes, with the agreement of the parties, these current contracts with PCS providers can be revised to

---

[17] Statement of Professor Jerry A. Hausman, para. 37 ("Hausman Statement"), attached hereto as Exhibit B.

include Mutual Compensation arrangements, as can all existing contracts. There is no urgency to revise these arrangements. Most PCS providers are just beginning to establish their infrastructure networks, and few have begun to operate. In the near term, their traffic volumes will be very low. Moreover, the need for change is not urgent because, as Professor Hausman points out, "[t]he future success of PCS is not affected by interconnect prices."[18] Dr. Hausman explains:

> No economic reason exists to grant a subsidy to PCS by using a Bill and Keep approach because the future success of PCS is not affected by interconnect prices. First, note that numerous large corporations including AT&T, Sprint, AirTouch, and a number of the RBOCs have invested in buying PCS licenses in the FCC auction. These companies have invested over $7 billion and are committed by their license terms to construct PCS networks. Thus, the entry decision has been made, and this decision will not be reversed unless a near catastrophic economic downturn occurs. As with almost all telecommunications services, PCS technology leads to relatively high fixed costs and relatively low marginal costs in operating a PCS network. The entry decision will create significant economic incentives to expand output among PCS providers.[19]

Therefore, even if our current access charge-based interconnection arrangements were less satisfactory than they are, the public interest would not require immediate "interim" changes in the arrangements.

The emergence of local exchange competition makes this a particularly inappropriate time for the Commission to rush into the adoption of an uneconomic approach for interconnection. As Professor Hausman explains, if LECs price

---

[18] Hausman Statement, para. 59.
[19] Id.

interconnection unreasonably high, CMRS providers will seek out interconnection arrangements with other providers.[20] We could not afford to jeopardize our competitive position in that manner. On January 1, 1996, the CPUC authorized local competition in California, and during March of 1996 we expect full resale competition to begin. The CPUC has authorized 32 Competitive Local Carriers ("CLCs") to provide local exchange service in California, and that number will rise to approximately 65 when resellers are included. Pacific Bell has issued nearly 200 NXX codes to CLCs in California. Local service competition is spreading quickly not only in California but nationwide and will soon skyrocket. For instance, on February 22, 1996, Sprint and its three cable TV partners confirmed that they plan to introduce local and wireless phone service in 20 to 25 markets by the end of the year.[21] If we and other LECs were to treat CMRS providers unfairly, we would be providing these numerous local competitors all the more incentive to provide alternative interconnection arrangements. Instead, we are striving to meet the needs of CMRS providers so that they will build long-term business relationships with us.

In our negotiations with CMRS providers, we have a model contract[22] but offer varied interconnection choices many of which CMRS providers have requested. We negotiate our contracts to meet the individual needs of a CMRS provider. The agreements typically include "most favored nation" clauses so that any other customer in a similar situation can obtain the same conditions. Moreover, instead of the model

---

[20] See id. at paras. 11 and 51.

[21] BC-Telecom-Sprint, Reuters, February 22, 1996.

[22] We have attached as Exhibit C the service descriptions, rate structures and rates from our model contract, and the model contract itself is available upon request.

contract, a few CMRS providers have chosen tariffed, intrastate FGD access service for mobile-to-land termination.

This CMRS interconnection process is similar to that ordered by the CPUC for local competition with CLCs. One important difference, however, is that for our interconnection with CLCs the CPUC ordered Bill and Keep as "a preferred outcome" for local calls only, on an interim basis for one year, while hearings take place later this year to determine the permanent arrangement. For toll calls, the CPUC imposed intrastate switched access charges as the compensation arrangement. We opposed Bill and Keep for local calls and still believe it is a mistake. Each party should pay the costs that it causes on the other's network. We recently negotiated a Mutual Compensation arrangement for both local and toll calls with MFS which, with some modifications, the CPUC approved.[23] We believe that this arrangement is far superior to Bill and Keep, because the Mutual Compensation arrangement fairly compensates each company for the costs incurred to terminate calls on its network whether or not traffic flow is balanced. We expect that traffic flow between CLCs and LECs will be unbalanced in the beginning months of local competition. But we expect that this imbalance will even out over time as CLCs begin to grow and more traffic flows from the LEC's network to the CLC. But the situation is more extreme for traffic flowing between wireless and wireline, which has maintained a very large traffic flow imbalance that is expected to remain for years. This makes Bill and Keep for CMRS-to-LEC

[23] The agreement with MFS demonstrates that Bill and Keep is not needed for new local service entrants.

interconnection particularly harmful. It would create severe harm to consumers and perverse incentives in the industry, as we discuss below.

C. THE COMMISSION'S INTERIM PROPOSAL FOR "BILL AND KEEP" WOULD CAUSE SEVERE HARM TO CONSUMERS AND THE INDUSTRY

Mutual Compensation, not the Commission's proposed "Bill and Keep," is the proper next step for LEC-to-CMRS interconnection arrangements. As Professor Hausman explains:

> The first principle of an economic approach to interconnection charges is mutual compensation. The basic economic principle is that since interconnection causes a company to incur costs, the company should be compensated for its expenditure. Otherwise, a competitor will not necessarily make the economically efficient investment decision, but it instead will attempt to use an existing network to minimize its own costs while causing the existing network to incur greater costs.[24]

By pricing termination at zero, Bill and Keep would create numerous economic distortions that would harm consumers and the industry.[25]

Bill And Keep Would Encourage Arbitrage

Bill and Keep would encourage arbitrage by subsidizing one technology, at the expense of others. For instance, when an IXC has a wireless affiliate or an agreement

---

[24] Hausman Statement, para. 41, attached hereto as Exhibit B.

[25] Id. at paras, 6-18, 14-40, 43-44, 62-66.

with a wireless entity, all the IXC's normal wireline terminating traffic could be routed via the wireless network for call completion to the LEC network and avoid normal access charges.

Dr. Hausman provides examples of how this may occur:

> Sprint has announced construction of a nationwide PCS network and AT&T will have a combined national PCS and cellular network. Both of these companies could switch significant amounts of their mobile or even landline long distance traffic to their PCS and cellular switches (MTSOs), and then terminate the traffic for free on the LEC network. These companies could thus avoid paying terminating access fees. Given the significant percentage of costs that access creates for IXCs, this strategy would be very attractive and would be a devastating outcome for the LECs. Note that the strategy would not use any airtime or spectrum which is the scarce resource, but would only need a mobile switch to interconnect the traffic to the LEC network.[26]

<u>Bill And Keep Would Discourage Investment And Innovation</u>

The offering of free terminating interconnection by LECs under Bill and Keep would leave CMRS providers with no economic incentive to expand parts of their networks where they can instead get a "free ride" on LEC investment.[27] In addition, Bill and Keep would discourage CLCs and other competitors from building facilities for termination of CMRS traffic, since they could not compete with a LEC price of zero. Moreover, because Bill and Keep would not provide LECs the opportunity to recover costs, LECs would have the incentive to offer only lower-cost options for

---

[26] <u>Id.</u> at para. 21.
[27] <u>Id.</u> at paras. 18-19.

interconnection with fewer features.[28] Accordingly, Bill and Keep would discourage optimal levels of investment and the innovation of new services and technologies.[29]

Bill and Keep Would Create An Unneeded Subsidy For CMRS Providers

In California, approximately 83% of CMRS traffic originates on the wireless networks and terminates on the wireline networks, while only approximately 17% of the traffic flows the other way.[30] Because of this traffic flow imbalance of over four to one, giving away terminating interconnection would create uncovered costs for LECs that are over four times greater than the uncovered costs for CMRS providers. Moreover, the LECs' terminating costs are not close to zero, contrary to Brock's figures upon which the Commission tentatively relies.[31] See Sections II - A-2 and 3 below. In addition, Professor Hausman explains why LEC-to-CMRS interconnection costs are likely to continue to increase:

> Furthermore, I expect large increases in PCS and other CMRS interconnection traffic since it is growing at the rate of 40% per year, with even higher growth rates with new CMRS providers beginning operation. Thus, 'excess capacity' formerly available from the fill engineered into the landline networks will be expended quickly with a likely increase over time in interconnection costs.[32]

---

[28] Id. at para. 17.

[29] Id. at paras. 16-19 and 63.

[30] Our traffic flow is approximately 92.6% mobile-to-land for wireless traffic that we record and bill to the CMRS provider. This traffic flow is approximately 86.9% mobile-to-land if we add an estimated amount of local traffic that we currently do not record or bill. The traffic flow is approximately 83.1% mobile-to-land when we also include traffic billed to an IXC.

[31] NPRM, paras. 60, 61, n. 78.

[32] Hausman Statement, para. 32.

The Commission suggests that the LECs could recover costs through new charges billed to our end users. This is much easier said than done. The requirements for billing system changes, network changes to identify calls to which new charges apply, and regulatory approvals by states will require time and cannot be accomplished immediately as would be required for an interim Bill and Keep policy.

Because of the traffic imbalance and its resulting cost imbalance, Bill and Keep would subsidize CMRS providers.[33] By reducing the LECs' recovery of shared and common costs of their networks, Bill and Keep would place pressure on rates for residential ratepayers and other customers to make up that recovery. There is no public interest rationale for this cross-subsidy. Thus, Bill and Keep would be contrary to sound economic principles under which the party that causes costs should pay for their recovery, and would be contrary to the goal to maintain universal service.[34]

Bill And Keep Would Create Long Term Problems

The Commission should avoid "the disease" of "market failures" by rejecting a policy based on Bill and Keep.[35] Once established on an interim basis, it may be very difficult to remove because it will give "the recipients of the subsidy reason to fight against its removal."[36] Bill and Keep may become like the "temporary" ESP exemption

---

33 Hausman Statement , paras. 24-25.

34 See id.

35 See id. at para. 14, quoting Paul Samuelson and W. D. Nordhaus.

36 Id. at para. 20.

from access charges that the Commission created to avoid "rate shock" in 1983, and which continues today in spite of the Commission's subsequent reviews of the exemption and proposal to remove it.[37] In addition, because Bill and Keep would lead to "misguided investment by firms," the distortions of an interim Bill and Keep policy "are likely to remain for a considerable period of time, even after Bill and Keep has been eliminated in favor of a more rational economic pricing framework."[38]

In summary, the decision concerning Bill and Keep is not a "close call."[39] Bill and Keep does not satisfy Commissioner Ness' concern that there be "rough justice."[40] Professor Hausman points out, "Non-price systems as proposed by the Commission in the NPRM have been tried and found to create large amounts of economic inefficiency in Eastern Europe and the former Soviet Union."[41] Bill and Keep "will lead to a waste of society's resources which is among the worst possible outcomes of government policy."[42]

---

[37] Amendment of Part 69 of the Commission's Rules Relating to Enhanced Service Providers, CC Docket No. 87-215, Notice of Proposed Rulemaking, 2 FCC Rcd 4305 (1987); Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture, CC Docket No. 89-79, Report and Order, 6 FCC Rcd 4524 (1991).

[38] Hausman Statement, para. 63.

[39] Id. at para. 62.

[40] Separate Statement of Commissioner Susan Ness, p. 1.

[41] Hausman Statement, para. 44.

[42] Id. at para. 16.

D. <u>WHETHER OR NOT THE COMMISSION ORDERS BILL AND KEEP, ANY "INTERIM" CHANGE WOULD HARM THE INDUSTRY AND THE PUBLIC</u>

The Commission's proposal to order an interim approach for LEC-to-CMRS interconnection would violate Commissioner Ness' admonition against "throwing caution to the wind."[43] No matter how the Commission might structure an interim approach, that approach would interrupt our existing arrangements which are based on access charge principles. In these arrangements, we depend on compensation for originating and terminating access in order to have an opportunity to recover our costs. The charges have been negotiated as integrated packages, and we expect that revisions in the charges between the carriers will necessitate revisions in charges to end users.

Our most popular CMRS interconnection arrangement provides an example of why we expect to need changes in end user charges in order for us to change LEC-to-CMRS interconnection arrangements to either Bill and Keep or Mutual Compensation. Most CMRS providers in California purchase Type 2A access-tandem interconnection from Pacific Bell. When we negotiated this arrangement, in order for the CMRS providers to increase traffic terminating to their networks, they requested pricing that allows landline end users to call CMRS end users from anywhere in a LATA without paying toll rates. This feature allows residential end users of Pacific Bell and of LECs that we pool with to call a CMRS end user anywhere in the LATA with no charges in addition to those for basic flat-rate local service, which Pacific Bell prices at $11.25 per month. For instance, if a Pacific Bell residential flat-rate subscriber in

---

[43] Separate Statement of Commissioner Susan Ness, p. 2.